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8 UNITED STATES DISTRICT COURT
9 DISTRICT OF ARIZONA

10 Barbara Borchers and Jerald S. Chesler, as
11 Trustee of the Betty D. Olson Revocable
12 Trust and The Olson Living Trust,

13 Plaintiffs,

14 v.

15 The Vanguard Group, Inc. and Vanguard
16 Marketing Corporation,

17 Defendants.

No. CV08-02138-PHX-ROS

**PLAINTIFFS' RESPONSE IN
OPPOSITION TO THE
DEFENDANTS' MOTION FOR
SUMMARY JUDGMENT.**

18 Plaintiffs, BARBARA BORCHERS and JERALD S. CHESLER, as Trustee of the Betty
19 D. Olson Revocable Trust and The Olson Living Trust, submit this Response to the Motion for
20 Summary Judgment filed by Defendants, THE VANGUARD GROUP, INC. and VANGUARD
21 MARKETING CORPORATION (hereinafter "Vanguard").

INTRODUCTION

22 Defendant Vanguard is a mutual fund. The accounts in question were investment
23 accounts, not bank accounts. Vanguard's witnesses admitted at deposition that Vanguard is not a
24 bank. The statutory section relied on in defendants' motion, A.R.S. §47-4406(F), by its own
25 terms, only applies to a "bank." Therefore, under the testimony of defendants' own witnesses,
26 defendants' legal defenses under A.R.S. §47-4406(F) do not apply. That is why defendants'
motion refers to Vanguard as a "financial institution." Vanguard attempts to broaden the scope

1 of the statute beyond its application to a “bank.” The problem with defendants moving to
2 another level of generalization is that the statute does not apply to a “financial institution.” It
3 only applies to a “bank.” To be sure, the Vanguard mutual fund provided check writing
4 privileges so that customers could withdraw money from their investment accounts. But that did
5 not make Vanguard a “bank” under the statute. The recognition of that fact, and legal conclusion
6 that flow from that fact, defeat the motion for summary judgment.

7 But even assuming, *arguendo*, and contrary to the language of the statute, that the
8 strictures of A.R.S. §47-4406(F) apply to an investment account at a mutual fund, summary
9 judgment is still inappropriate because plaintiffs called and met with Vanguard employees
10 numerous times about the forgery issue. The meetings began in 2005. The tapes of those phone
11 calls were produced by Vanguard in this case and are submitted with this Response. Moreover,
12 Vanguard admittedly failed to provide the necessary forms to plaintiff that it routinely gave to
13 customers so that a customer could report specific forged checks. And last, but not least,
14 plaintiffs met with a Vanguard representative who showed the plaintiffs the checks that they
15 believed were forged. So Vanguard itself had, through its security apparatus, identified
16 suspicious checks. To that end, Vanguard informed the plaintiffs that it would “flag” their
17 investment accounts, but then it failed to do what it had undertaken to do. Simply put, that was a
18 lack of due care that creates triable issues of fact precluding summary judgment.

19 **STATEMENT OF FACTS**

20 The 30(b)(6) deponent designated by Vanguard was William Matysik, a senior
21 fraud investigator. He listened to 20 to 25 phone calls between Betty Olson, her daughter,
22 Barbara Borchers and Vanguard representatives (Pltf. SSOF, ¶45-46).

24 Vanguard asked its customers to fill out its Statement of Forgery, which
25 specifically identifies by CWR number exactly the check, the amount, the payee, what
26 fund it came from, and that she did not receive any direct benefit from the check. Each

1 check required a separate Vanguard Statement of Forgery pursuant to Vanguard's
2 policies and procedures, but Vanguard did not send the required documents, such as the
3 Statement of Forgery, to Betty Olson, and the Vanguard representative did not know if
4 she was asked to identify forged checks (Pltf SSOF, ¶47-48). It was Vanguard's policy
5 and procedure to complete the Statement of Forgery identifying the specific checks that
6 were forged. Vanguard's policy was that if a client calls in then Vanguard is going to ask
7 them to identify by check number which checks they are speaking about.. The fraud
8 team then completes the Statement of Forgery listing the checks (Pltf. SSOF, ¶49-50).

11 According to the Vanguard deponent representative, there was no allegation made
12 that checks were being written that were not authorized by the client, Betty Olson, which
13 allegation triggers the Statement of Forgery procedure (Pltf. SSOF, ¶50-51). But one
14 document did have the amounts of checks that was sent to Vanguard (Pltf. SSOF, ¶51-
15 52).

17 The representative deponent did not know if forged checks were reported. He did
18 know that Shelly Wilson of Vanguard met with Betty Olson in 2005 at Vanguard's
19 Scottsdale office (Pltf. SSOF, ¶55-56).

21 Vanguard is not a bank. It is an investment company in the mutual fund business
22 The accounts were mutual fund accounts, investment accounts (Pltf. SSOF, ¶57-58, 64).

23 Shelly Wilson was and is a customer service representative in Scottsdale. In 2005
24 Betty Olson and Barbara Borchers alerted her, as a Vanguard employee, that they were
25 afraid of someone writing checks, signing the checks. Betty Olson told Shelly Wilson
26

1 that her daughter Barbara Borchers was authorized to deal with the check writing issue.
2 Barbara and Betty Olson told Shelly Wilson that there were checks that Betty Olson had
3 not signed. Wilson followed Vanguard policy and notified the fraud department that the
4 client alleged there were checks she was not signing (Pltf. SSOF, ¶¶59-61).

6 Barbara and Betty also came in to see Shelly Wilson at the Vanguard office.
7 Shelly does not remember whether she showed Barbara forged checks (Pltf. SSOF, ¶¶62-
8 63). Wilson said it was apparent that the checks in question did not have Betty Olson's
9 signature on them because the signatures did not match when compared against Betty's
10 signature card on the computer.
11

12 ARGUMENT

13 **I. VANGUARD IS NOT A BANK UNDER THE** 14 **ARIZONA UCC. IT IS AN INVESTMENT COMPANY**

15 Defendant relies on A.R.S. §47-4406(F), which provides in relevant part as follows:

16
17 “F. Without regard to care or lack of care of either the customer or
18 **the bank**, a customer who does not within one year after the statement or items
19 are made available to the customer (subsection A of this section) discover and
20 report the customer's unauthorized signature on or any alteration on the item is
precluded **from asserting against the bank** the unauthorized signature or
alteration....”

21 (emphasis added).

22 Vanguard offers no explanation in its motion for summary judgment as to why a statute
23 that plainly applies to a “bank” also applies to a mutual fund. Vanguard's conclusory claims of
24 being a “financial institution” do not bring it within the statute it invokes. For that reason alone,
25 summary judgment should be denied because Vanguard cannot demonstrate that it is entitled to
26 judgment as a matter of law.

1 **II. EVEN IF VANGUARD IS A BANK UNDER THE**
 2 **ARIZONA UCC. IT IS NOT RELIEVED OF LIABILITY.**

3 Defendants argue that plaintiffs are precluded from asserting against Vanguard a check in a
 4 statement, on the grounds that the signature was forged or that the instrument was altered, if
 5 Vanguard establishes that the plaintiffs failed to comply with their duties with respect to such
 6 matters, where the customer's breach of duty has resulted in loss to the bank. However, even if
 7 Vanguard was a bank, the Uniform Commercial Code provides that the preclusion does not
 8 apply if the customer establishes that the bank failed to exercise ordinary care to detect
 9 unauthorized signatures or alterations. *Aikens Const. of Rome, Inc. v. Simons*, 284 A.D.2d 946,
 10 727 N.Y.S.2d 213 (4th Dep't 2001)(Even if bank customer failed to notify bank of check
 11 forgeries within 14 days after customer received bank statement that included first forged check,
 12 bank would not be protected from liability if customer could establish that bank did not observe
 13 standards of ordinary care). The customer's breach of his duties as set forth in the Code has no
 14 effect if it is established that the bank did not exercise ordinary care. Two other subsections of
 15 UCC § 4-406, A.R.S. §47-4406(D) and (E), establish the legal structure within which the bank's
 16 and the customer's conduct is evaluated. A.R.S. §47-4406(D) states that:

19 "D. If the bank proves that the customer failed, with respect to an item, to
 20 comply with the duties imposed on the customer by subsection C of this section,
 the customer is precluded from asserting against the bank:

- 21 1. The customer's unauthorized signature or any alteration on the item, if the bank
 22 also proves that it suffered a loss by reason of the failure; and
- 23 2. The customer's unauthorized signature or alteration by the same wrongdoer on
 24 any other item paid in good faith by the bank if the payment was made before the
 25 bank received notice from the customer of the unauthorized signature or alteration
 and after the customer had been afforded a reasonable period of time, not
 26 exceeding thirty days, in which to examine the item or statement of account and
 notify the bank."

1 The next subsection, A.R.S. §47-4406(E), is implicated if the bank satisfies the elements
 2 of A.R.S. §47-4406(D). If that occurs, subsection (E) then governs, which states that:

3 “E. If subsection D of this section applies **and the customer proves that**
 4 **the bank failed to exercise ordinary care in paying the item and that the**
 5 **failure substantially contributed to loss, the loss is allocated between the**
 6 **customer precluded and the bank asserting the preclusion** according to the
 7 extent to which the failure of the customer to comply with subsection C of this
 8 section and the failure of the bank to exercise ordinary care contributed to the
 9 loss. **If the customer proves that the bank did not pay the item in good faith,**
 10 **the preclusion under subsection D of this section does not apply.**”

11 Defendants’ motion fails to mention or analyze the contours of subsections (D) and (E). Nor
 12 does Vanguard offer any evidence to this Court to show that “it suffered a loss by reason of the
 13 failure” under A.R.S. §47-4406(D)(1). Nor does it offer any evidence on the notice issue under
 14 A.R.S. §47-4406(D)(2), although from plaintiff’s point of view Betty Olson and her daughter
 15 Barbara Borchers notified Thus, all of the subsections § 4-406 govern the situation where a
 16 Bank honors a forged check, not just the subsections cited by the defendants in this case. *Nu-*
 17 *Way Services, Inc. v Mercantile Trust Co. Nat. Asso.*, 530 S.W.2d 743 (Mo. App. _____).

18 As the Supreme Court set out in *Schoenfelder v. Arizona Bank* (1990) 165 Ariz. 79, 796 P.2d
 19 881, the bank must show how customer’s delay in reviewing statement and notifying bank of
 20 forgeries resulted in the loss to the bank. In order to assert the defense of customer negligence in
 21 examination of statements as defense to action by customer to require bank to recredit account
 22 for payments made on checks containing forged signature, the bank must affirmatively establish
 23 that customer’s negligence in inspecting statements or giving notice of forgeries caused the
 24 loss. *Id.*

25 This the defendant Vanguard failed to do in its motion. In re L & D Interests, Inc., 350
 26 B.R. 391 (Bankr. S.D. Tex. 2006); *Phariss v Eddy* (1991, Iowa App) 478 NW2d 848, 17

1 UCCRS2d 181; Biltmore Assoc., Ltd. v Marine Midland Bank, N. A. (1991, 4th Dept) 178 App
2 Div 2d 930, 578 NYS2d 798, 17 UCCRS2d 179; Lawyers' Fund for Client Protection of State of
3 N.Y. v. Gateway State Bank, 692 N.Y.S.2d 583 (Sup. Ct. 1999). There is no doubt that a bank
4 must use reasonable and proper methods to detect forgeries. Travelers Indem. Co. v. Good, 325
5 N.J. Super. 16, 737 A.2d 690 (App. Div. 1999), which issue is a question of fact. National
6 Accident Ins. Underwriters, Inc. v. Citibank, F.S.B., 243 F. Supp. 2d 763 (N.D. Ill. 2002).

7 It is apparent that Vanguard was informed by plaintiff in 2005, by its own admission, that
8 forgeries were occurring. Vanguard undertook to "flag" the account and then failed to do so.

9 For those reasons, the motion should be denied.

10 Dated: December 16, 2010
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CERTIFICATE OF SERVICE

☒ I hereby certify that on December 16, 2010, I electronically transmitted the attached document to the Clerk's Office using the CM/ECF System for filing and transmittal of a Notice of Electronic Filing to the following CM/ECF registrants:

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